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ABSTRACT

In November 1978, Idaho voters approved an initiative that limited property taxes to 1 percent of a property's 1978 market value and that limited the property's growth in market value to 2 percent per year. Due to the initiative's imprecise wording and incompatibility with Idaho statutes, the 1979 Idaho Legislature passed two bills designed to clarify the initiative and enact it into law and to rewrite the school finance statutes to conform to the new limitations. These two bills included limitations on the amount of taxes taxing districts and school districts could levy, with the provision that school district voters could approve increased levies for school finance only. The state's share of the costs of education rose as a result of the changes from 65 percent in 1978-79 to 75 percent in 1979-80. Among the issues remaining to be resolved are determining how revenue from property taxes should be divided among taxing jurisdictions, since taxing district boundaries overlap; whether voters will be allowed to override limitations in the future; and whether underassessed residential property will be reassessed to full 1978 values, possibly resulting in higher tax bills for homeowners than were faced prior to the reforms. (Author/PGD)

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A BRIEF ANALYSIS OF THE IMPLEMENTATION OF IDAHO'S 1% INITIATIVE

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THE IMPLEMENTATION OF IDAHO'S 1% INITIATIVE

On November 7, 1978 voters in the state of Idaho approved a 1% property tax limitation Initiative by a 58.3% margin. Passage of this 1% Initiative makes Idaho the only state outside of California to have approved such a limitation.[1] Like California's Proposition 13, the 1% Initiative limits the amount of property taxes that can be collected annually from a piece of property to 1% of the market value of that property. Unlike Proposition 13, Idaho's 1% Initiative was not a constitutional amendment, but rather a statutory change. This significant difference gave the Idaho Legislature more opportunity than was available to the California Legislature to temper the effects of the limitation. Although most Idaho legislators went to Boise in January 1979 committed to the spirit of the 1% Initiative, all were prepared to correct a number of obvious problems that existed in its original language. This paper is designed to provide readers with background information on: (1) the important components of the 1% Initiative; (2) the actions of the 1979 Idaho Legislature; and (3) areas where future legislative action will be required, particularly as these issues relate to public education.

Idaho's 1% Limitation

As passed by the voters, the 1% Initiative did the following:

- Limited property taxes to 1% of the "actual market value"
- Exempted special assessments and bonded debt approved by the voters prior to the passage of the measure
- Limited the growth in market value of property to 2% per year unless it changed hands, at which point it could be reassessed

[1] Nevada has also passed a 1% property tax limitation. However, it must be approved by the voters again in 1980 before it becomes effective.

- Required two-thirds approval of both houses of the Legislature to enact new state taxes
- Allowed local taxing districts to enact replacement taxes (except property taxes) by a two-thirds vote of the electorate
- Stipulated that it would become effective on October 1, 1979

Early estimates indicated that the 1% Initiative would reduce property tax collections in Idaho by 60%. This would amount to a reduction of $126 million out of total property tax collections of $211 million in 1977-78. Unlike California, Idaho does not have a large budgetary surplus available to "bail-out" local taxing districts. One of the major reasons for this was legislation passed in 1977 which required that any budgetary surplus in excess of 2% of the general fund be used to reduce the county levy for the support of schools. In other words, state surpluses were already being used to relieve property taxes. Another surprising factor in the success of the 1% Initiative in Idaho is the fact that property taxes only amounted to about 1.57% of market value as compared to other states where property taxes are as high as 4% of market value.

There were many serious problems in the drafting of this Initiative. In many instances the language did not reflect current Idaho statues and it contained a number of references that are not defined in Idaho law, making the actual meaning of those passages unclear.

For example, the Initiative stated that taxes would be limited to 1% "actual market value." This term does not appear in Idaho statutes and its meaning is unclear. The Initiative further defined "actual market value" by saying that "actual market value" shall be determined by the county assessor, and in the case of real property--shall be the "actual use" of the property. Analysis of this language indicated that the term

"actual use" could be construed to mean that vacant property would carry no value and thus wouldn't generate any property tax revenue. This section of the Initiative also stated that "actual market value" would be the county assessor's evaluation shown on the 1978 tax assessment and could only be changed if the property changed hands. The assessor was allowed to correct "errors" prior to 1978 and bring undervalued property up to 1978 levels. Property values were allowed to increase at a rate not to exceed 2% per year until the property was sold. The Initiative also required a two-thirds vote in both houses of the Legislature to approve any new state taxes. This section conflicted with the Idaho Constitution which allows the Legislature to enact new state taxes with a majority vote of both houses.

Another serious problem with the 1% Initiative was the fact that it became effective "for the tax year beginning on October 1, following passage...." This was troublesome because there is no tax year in Idaho that begins in October 1. There was considerable debate following the passage of the 1% Initiative as to whether the Initiative should become effective on January 1, 1979 or January 1, 1980. Many supporters of the 1% Initiative felt that by waiting until 1980, the Legislature would not be meeting the mandate of the people.

Faced with the task of enacting legislation which maintained the spirit of the 1% Initiative, while at the same time cleaning up its language so it was compatible with Idaho law, the 1979 Legislature responded by enacting two bills--House Bill (HB) 166 and House Bill 306. The two bills, which were signed into law by Governor John Evans, are the basis for the 1% limitation in Idaho.

The Legislature's Response

The mechanism used by the Legislature to enact the 1% Initiative into law was HB 166. HB 306 was designed to rewrite the school finance statues so they conformed with the new property tax limitation. The major components of each bill are described below.

Section 1 of HB 166 limits property taxes to 1% of "market value" and excludes from this limitation all bond issues approved both before and after the passages of the 1% Initiative.

Section 1 also states that all property in the state shall be appraised at its 1978 market value (value on December 31, 1978) by January 1, 1980. It states that all new property shall be placed on the assessment roll at its 1978 value, even if it is built in some future year. Additionally, HB 166 attempts to clear up the problem created by the statement that all real property shall be assessed at the "actual" use of the property, by changing that statement to read "the actual and functional" use of the property. This change is intended to allow the taxation of vacant property, although there is still a great deal of confusion over the definition of "functional use" of property.

The final paragraph of Section 1 states that increases in market value of property may not exceed 2% a year. However, this section does not allow a revaluation of property when it changes hands. This means that property values will not grow more than 2% a year, no matter how many times a piece of property changes ownership. Finally, there is some confusion over how new property will be added to the assessment rolls. It is unclear whether new property is to be placed on the rolls at its 1978 value, or at its 1978 value plus 2% per year up to the year in which

it was constructed. This section will probably have to be clarified either through legal challenge, or through a statutory revision.

Section 2 of HB 166 stipulates that no taxing district in the state may certify a budget for 1979-80 or 1980-81 which collects more property taxes than were collected during Fiscal Year 1978-79. (HB 306 allows school districts to exceed this with a majority vote.) This effectively freezes local property tax collections at the 1978-79 levels unless voters approve larger increases for school districts. The actual 1% limit will take effect for the first time in Fiscal Year 1981-82.

Section 3 of the HB 166 requires that the 1978 market value be used for assessment purposes in Fiscal Year 1980-81, requires county assessors to submit a plan to reassess property within their county to the State Tax Commission, and gives the Tax Commission the authority to monitor each county's implementation of the plan. If a county fails to meet its plan, the Tax Commission is empowered to take over and do the task itself. Finally, the bill removes the section of the Idaho code defining assessed valuation as 20% of market value. This definition is not needed since 1978 market value will be used for assessment purposes in the future. The section changing the definition of assessed valuation really has no effect on property tax collections, only on stated tax rates. For example, a property tax limitation of 1% of full market value translates to a maximum tax rate of 10 mils, or $10 per thousand. If assessed valuation is defined as 20% of market value, then a property tax limit of 1% of market value translates to a maximum tax rate of 50 mils or $50 per thousand.

The second piece of Legislation, HB 306, dealt specifically with school districts. HB 306 required that each school district reduce its levy by 7 mils. This reduced the maximum levy authority of a school district without a vote from 27 mils to 20 mils. In addition, since HB 166 froze property tax collections at 1978-79 levels, any district that was able to raise more than it raised in 1978-79 with its reduced levy was forced to reduce its levy even further. In effect, there is a double limit on how much a school district can raise through property taxes. Districts may not levy more than 20 mils, and their revenues from property taxes are frozen at 1978-79 levels. In no situation can a district raise more than last year or levy more than 20 mils. This limit may, however, be exceeded by a majority of the district's voters. In addition HB 306 eliminated the 4 mil county levy that had previously been part of the school finance formula. To compensate school districts for the lost revenue from this 11 mil reduction (7 districts and 4 counties), and to provide for small increases in expenditures for inflation, the Legislature appropriated almost $30 million in additional aid to school districts. Even with this $30 million, there are 16 districts that will receive fewer dollars in 1979-80 than they did in 1978-79. To alleviate this problem, an additional $1 million was set aside as a "hold-harmless" appropriation. The State Board of Education is empowered to distribute this money to school districts that are unable to generate the same amount of revenue as was available to them during 1978-79.

The effect of these additional appropriations was to increase the state share of the costs of education from 65% in 1978-79 to 75% in 1979-80.

Areas Requiring Further Consideration

While many of the important issues surrounding Idaho's 1% Initiative have been dealt with by the Legislature, there are still many others to be considered during the 1980 Legislative session. Primary among them is how the revenue from the property tax should be divided among taxing jurisdictions. Since taxing district boundaries overlap, a certain piece of property may be in more taxing districts than another piece of property located elsewhere in the same county. In addition, the Idaho Constitution requires that a taxing district levy a uniform tax rate on all property within its jurisdiction. This means that tax rates for all taxing districts must be established, so that no piece of property is subject to taxes higher than 1% of market value. The method most frequently discussed to achieve this in Idaho is to find the highest tax code area in each county and assign each taxing district a tax rate proportional to its current share of the total. Then all similar taxing districts in each county would also receive that proportion of the total tax collections. For example, if city A in the highest tax code area of county X has a tax rate that represents 20% of the total tax rate in that tax code area, then the maximum tax rate for all cities in county X would be 2 mils, or 20% of the allowable 1% maximum property tax. (NOTE: This would be 10 mils if a 20% assessment ratio were maintained.)

Use of such a proportional distribution of the tax rates would result in many properties being taxed at less than 1% of market value. Because a piece of property may be located in county X, but not in an incorporated city. In that case the 2 mils reserved for cities would not be levied against that piece of property, and the tax rate would be no higher than 8/10 of 1% of market value or 8 mils.

One possible option to the proportional method that has also received some attention is to leave school district levies at the current level and then assign proportional rates to the rest of the taxing districts based on the portion of 1% that is left over after the school district levy is subtracted from the total.

The current legislation allows local school districts to override the current 20 mil limit on property taxes with a majority vote. The 1980 Legislature will have to decide whether or not school districts, or any taxing districts, will be allowed to ask voters to override the 1% limitation. In addition, the Legislature will have to decide whether a majority vote can override the 1% limitation or if a two-thirds vote will be required.

One final issue which is likely to cause considerable difficulty for school officials in the future is the reassessment of property to 1978 values. Many residential properties in Idaho are tremendously undervalued at the present time. In fact, the general pattern in most (but not all) Idaho counties is for utility property to be assessed at over 100% of market value, business and commerical property to be assessed at almost 100% of market value, and residential property to be assessed at about one-third of market value. If all property is reassessed at 100% of market value, then there will be a shift in the burden of the property tax from utility, business and commerical property to residentail property. The current undervaluation of residential property, combined with this shift may mean that many homeowners will not receive significant tax relief and, in fact, may actually have higher tax bills after the 1% limitation is enacted.

One solution to this situation is to classify property and levy taxes against a lower percentage of the market value of residential property than of commerical, business and utility property. Unfortunately, the Idaho Supreme Court has ruled that such property classification would be unconstitutional. The implication of all this is that school districts will be faced with severely limited revenues due to the 1% limit, while at the same time, homeowners may not receive very much property tax relief. This could lead to very dim prospects for the approval of levy overrides; if the Legislature allows school districts to ask for such approval.

Conclusion

Although the Legislature has taken a number of steps to alleviate the problems caused by the 1% Initiative, there are a number of issues that must still be resolved. Local governments throughout the state will find their ability to raise needed revenues severely limited in the future and will probably have to reduce service levels. Because Idaho did not have a particularly high property tax burden (1.57% of market value last year) taxpayers may not receive as much relief as they expected. This is particularly true due to the inequities that currently exist throughout most of the state's property assessment. It is interesting to note that in Ada County (Boise) where a complete property reassessment took place two years ago, voter support for the 1% Initiative was extremely high. This was due, no doubt, to the fact that residential property owners received large increases in their assessments. If this pattern holds in other Idaho counties, there may be a clamor for further tax cuts--a situation which would only force school district expenditures already among the lowest in the nation, even lower.